

THE FINANCIAL SERVICES ROUNDTABLE



Testimony of

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on behalf of

The Financial Services Roundtable

Before the

United States House of Representatives
Financial Services Subcommittee on
Financial Institutions and Consumer Credit

on

The Joint Proposal by

The Board of Governors of the Federal Reserve System

and

The United States Treasury Department

To Allow Financial Holding Companies
and National Bank Financial Subsidiaries
to Engage in Real Estate Brokerage
and Real Estate Management Activities

May 2, 2001

Good Morning, Chairman Bachus, Ranking Member Waters, members of the Subcommittee. My name is Richard J. Parsons, I am Executive Vice President of Bank of America, and I am testifying on behalf of The Financial Services Roundtable. The Roundtable is a national association that represents 100 of the largest diversified financial services companies, including 64 commercial banking and thrift organizations, 12 insurance companies, seven securities or investment companies, and four other types of diversified financial services companies. A complete list of the Roundtable's members is attached. (*See Attachment A*). Member companies participate through their Chief Executive Officer and other senior executives nominated by the CEO.

Roundtable member companies provide fuel for the engine of our nation's economy, accounting directly for \$17 trillion in managed assets, \$6.6 trillion in assets, and \$462 billion in revenue, and providing 1.6 million jobs.

The Roundtable appreciates this opportunity to discuss the joint proposal of the Federal Reserve Board and the Treasury Department to permit financial holding companies and national bank financial subsidiaries to engage in real estate brokerage.

The Roundtable strongly supports adoption of the regulation for three reasons. First, permitting financial holding companies and national bank subsidiaries to enter the real estate brokerage business is good for consumers. Second, it is good for the financial services industry. Third, real estate brokerage is a financial activity consistent with the Gramm-Leach-Bliley Act.

Consumers Will Benefit From the Proposed Rule

The Roundtable strongly believes that consumers will be the real winners if the regulation is adopted. Adoption of the rule will increase competition in the brokerage industry. More competition means more consumer choice, lower prices, and better customer service.

Adoption of the rule is necessary to meet consumer demand for one-stop shopping for all their home buying needs. In 1999, a study of recent home buyers was conducted on behalf of the National Association of Realtors (“NAR”). (*See Attachment B*). According to this NAR study, 76 percent of home buyers said that getting all or some of their home buying services handled through one company was appealing. Eighty-one percent supported the idea of one-stop shopping for all of their home buying services and were evenly split on whether the best provider of such services would be a bank, a realtor, or a mortgage company, although a slight majority stated they would prefer a bank as the one-stop shopping provider. The NAR study concluded that 77 percent would consider using a bank for those one-stop shopping services in future transactions.

If the proposed rule is adopted, consumers will be able to receive in one location all the services necessary to buy a home: pre-approval for a mortgage loan; assistance in finding a home; a mortgage loan after a contract to purchase a home has been signed; and insurance for the property (including title insurance, property insurance, and private mortgage insurance) prior to closing. The consumer’s life will be simplified and services will be expedited. Many traditional real estate brokers have already responded to consumer demand for one-stop shopping and are offering mortgage and insurance services in addition to real estate brokerage services.

Opponents of the regulation contend that consumers are worried about their privacy when purchasing a home. Concluding that brokerage is a financial activity in fact enhances consumer privacy. While customers of financial holding companies and national banks are entitled to the GLB Act’s far-reaching privacy protections, customers of real estate brokers currently have no federal privacy protections. If adopted, the regulation will afford brokerage customers the same federal privacy protections now afforded to bank customers. Thus, real estate brokers will have to disclose their privacy policies to home buyers and will be prohibited from sharing certain nonpublic information about the home buyer with any nonaffiliated third parties unless the home buyer has been given notice and the opportunity to opt out of such information sharing.

Opponents also argue that allowing financial holding companies to offer real estate brokerage services could result in harmful tying and other coercive practices. This argument is easily refuted by the fact that many brokerages are already affiliated with mortgage lenders, insurers, thrifts, credit unions, and state banks, and there is no evidence of these harmful practices occurring.

Moreover, existing banking laws are more than adequate to preclude these types of practices within a financial holding company. Sections 23A and 23B of the Federal Reserve Act prohibit a bank from making below-market loans to any affiliates or subsidiaries, including those that would be engaged in real estate brokerage, and severely restrict a bank's ability to provide equity contributions and other support to the real estate brokerage affiliate.¹ Furthermore, Section 8 of the Real Estate Settlement Procedures Act² and the anti-tying provisions of Section 106 of the Bank Holding Company Act Amendments of 1970³ preclude any coercive practices against the bank's (or brokerage's) customers. A brokerage customer of a financial holding company will in fact enjoy greater protection than a brokerage customer of a less regulated competitor, such as a traditional real estate brokerage firm or finance company.

The Financial Services Industry Will Benefit From the Proposed Rule

Adoption of the regulation is prudent for the financial services industry. Traditional real estate brokers are now actively competing with banks and financial holding companies by offering financial services – in particular, loans and insurance. Of the ten leading real estate brokers cited by *Realtor* magazine, nine provide financial services and compete with financial holding companies by offering loans or insurance. According to the “1999 National Association of Realtors Profile of Real Estate Firms,” 56 percent of its residential real estate brokerage firms with more than 50 agents are involved in mortgage lending. (*See Attachment C*).

¹ See 12 U.S.C. §§ 371c, 371c-1 and 1828(j).

² 12 U.S.C. § 2607.

³ 12 U.S.C. § 1971, *et seq.*

Additionally, federal thrifts⁴ and credit unions⁵, as well as state-chartered banks in 26 states, are permitted to act as real estate brokers. (*See Attachment D for data on the states*). In fact, the only financial institutions that uniformly cannot engage in real estate brokerage are financial holding companies and national banks. We ask only that this playing field be leveled, and that financial holding companies and national banks be permitted to compete as well.

There is no evidence that consumers have been hurt in any way by the current involvement of these depository institutions in the real estate brokerage industry, and there is no evidence that depository institutions dominate the brokerage industry or enjoy significant market power. Prohibiting real estate brokers from affiliating with financial holding companies and national bank subsidiaries seems to be out of step with the current marketplace.

Moreover, brokerage poses little risk to the banking system. A real estate brokerage company does not act “as principal,” but rather acts in an “agency” capacity by being an intermediary in a transaction between a buyer and a seller. Banks have historically been permitted to conduct “agency” activities either directly or through affiliates. Financial holding companies are currently permitted to provide their customers with a wide array of agency services, including travel, securities, commodities, and insurance brokerage.

Real Estate Brokerage is a Financial Transaction Consistent with the Gramm-Leach-Bliley Act

Finally, the Roundtable believes that the proposed regulation is entirely consistent with the Gramm-Leach-Bliley Act of 1999 (“GLB Act”), which was designed to modernize and expand the financial services marketplace. The specific purpose of financial modernization, as stated in the preamble to the GLB Act, was to “*enhance competition in*

⁴ See 12 C.F.R. §§ 559.4(e)(3) (thrift service corporations), 584.2-1(b)(8) (thrift affiliates).

⁵ See 12 C.F.R. § 712.5(g) and (p).

the financial services industry by providing a prudent framework for the affiliation of banks, securities firms, insurance companies and *other financial service providers*, and for other purposes.” [emphasis added]

Title I of the GLB Act created the “financial holding company” structure and permitted financial holding companies to conduct a much broader range of financial activities than was historically permissible for bank holding companies. The GLB Act permits financial holding companies to engage in all activities that have been determined by the Federal Reserve Board to be “financial in nature,” or incidental or complementary to a financial activity.⁶ Given the historical experience of the Glass-Steagall Act and the practical limitations of creating a rigid regulatory structure, the GLB Act established a flexible framework that allows regulators to respond to changes in technology, the marketplace, and consumer demand. The GLB Act provides the Board, in consultation with Treasury, the authority to expand the statutory list of financial activities.⁷

In December 2000, the Board and Treasury issued a joint notice of proposed rulemaking to determine that real estate brokerage and real estate management activities are “financial in nature” or “incidental to a financial activity” and, consequently, permissible for financial holding companies and national bank subsidiaries. By issuing this proposal, the agencies are simply fulfilling their obligation under the GLB Act to ensure that financial holding companies and national banks have the ability to compete with other financial service providers. Assertions that the Board and Treasury may not rule on real estate brokerage are without basis under the GLB Act. Such an interpretation of the GLB Act would turn the clock back on financial modernization.

The broader scope of the “financial in nature” standard for non-bank activities of financial holding companies is reflected in both the legislative history of the GLB Act and the diverse range of activities that financial holding companies are currently

⁶ See Bank Holding Company Act § 4(k)(1)(A), (B) (12 U.S.C. § 1843(k)(1)(A), (B)).

⁷ See Bank Holding Company Act § 4(k) (12 U.S.C. § 1843(k)).

permitted to conduct. First, the Conference Report to the GLB Act states that “[p]ermitting banks to affiliate with firms engaged in financial activities represents a significant expansion from the current requirement that bank affiliates may engage only in activities that are closely related to banking.”⁸ Second, financial holding companies are currently permitted to conduct a broad range of activities that bank holding companies are prohibited from conducting, such as unrestricted securities underwriting, merchant banking, unrestricted insurance underwriting, unrestricted insurance agency, travel agency, and acting as finder.⁹ The financial services marketplace has changed dramatically in the past 30 years, and what may have been inappropriate for bank holding companies in the early 1970s may be entirely appropriate for the diversified financial holding companies of the early 21st century.

With respect to the permissibility of real estate brokerage under the GLB Act, the GLB Act permits the Board to define certain activities as “financial in nature,” including the “transferring ... for others financial assets other than money or securities.” The Roundtable believes that real estate brokerage is exactly that type of activity. Real estate is the largest financial asset owned by most consumers and is the most widely used source of collateral for consumers seeking credit. The purchase of real estate is the largest financial transaction for most consumers. For many, real estate is the largest source of individual wealth; the decision to purchase, sell, and finance real estate plays a significant part in retirement planning. Real estate is conferred special status under federal and state tax laws, distinguishing real estate from other large-ticket items. For these reasons, we believe that real estate is a “financial asset” and that brokerage is “financial in nature.”

In addition, the GLB Act defines as “financial in nature” all activities that involve “arranging, effecting, or facilitating financial transactions” for others.¹⁰ Real estate brokerage is part of the overall financial activity of helping a consumer receive pre-

⁸ H.R. Conf. Rep. No. 106-434, at 153 (Nov. 2, 1999).

⁹ See BHCA § 4(k)(4) (12 U.S.C. § 1843(k)(4)); 12 C.F.R. § 225.86(d)(1) (finder activities).

¹⁰ See Bank Holding Company Act § 4(k)(5)(B)(iii) (12 U.S.C. § 1843(k)(5)(B)(iii)).

approval for a mortgage loan, find a home, appraise the property, receive final approval for the mortgage loan, close the transaction, and insure the home with property insurance, title insurance, and, in certain cases, private mortgage insurance. Each of the services and products offered as part of the overall financial transaction are integrated with one another. Such integration is reflected in several ways. First, consumers frequently enlist the services of a real estate broker at the same time that they seek the products of a mortgage lender and an insurance agency. Second, consumers generally pay the loan fees, the realtor's commission, and the initial insurance premiums together at the closing. Third, the documents that consumers sign with respect to the mortgage loan, real estate brokerage, and the insurance generally cross-reference and are conditioned upon each other.

Moreover, in determining whether an activity is “financial in nature,” the GLB Act also requires the Fed to consider “changes in the marketplace in which financial holding companies compete” and whether such activity is “necessary or appropriate” to allow a financial holding company or its affiliates to “compete effectively with any company seeking to provide financial services in the United States.”¹¹ As highlighted earlier, approval of the regulation is both necessary and appropriate to allow financial holding companies to compete effectively with real estate brokerage companies, as well as with federal thrifts, credit unions, and state banks in 26 states.

As a result, the Roundtable firmly believes that real estate brokerage is “financial in nature,” consistent with the GLB Act. At the very least, the Federal Reserve Board and Treasury should find that it is “incidental to a financial activity.” Banks and financial holding companies are involved in virtually every other aspect of residential and commercial real estate transactions, ranging from rendering advice; acting as a finder; appraising the property; issuing abstracts of title and performing title searches; selling and underwriting hazard, title, and mortgage guaranty insurance; arranging or providing financing; providing loan closing, settlement, and escrow services; and securitizing

¹¹ Section 103(a), new Bank Holding Company Act (“BHCA”) section 4(k)(3)(A)&(D)(i).

mortgage loans or underwriting and selling mortgage backed securities. Clearly, acting as a real estate broker is incidental to the performance of these other real estate related services that are already considered to be “closely related to banking” or “financial in nature.”

Conclusion

In conclusion, we strongly support the regulation and believe that its adoption would be a win-win proposition for consumers and for the financial services industry. The regulation would allow financial services companies to build alliances with real estate brokerages, creating tremendous benefits for consumers, including one-stop shopping, lower prices, more choice, and increased competition.

The Roundtable respectfully asks the Committee to allow the Board and Treasury to complete their pending rulemaking. This process is an appropriate delegation of authority to the regulators, who have expertise and experience in this area and are fully equipped to consider all the substantive issues. This process allows for a decision on the merits.

Thank you. I will be glad to try to respond to any questions that Members of the Committee might have.